MINUTES
of the
LEGISLATIVE CONSUMER COMMITTEE
September 18, 2002
Missoula City Council Conference Room - Missoula, MT

COMMITTEE MEMBERS PRESENT

Senator Walter McNutt, Chairman
Senator Debbie Shea, Vice Chairman
Representative Tom Dell
Representative Roy Brown

STAFF PRESENT

Robert A. Nelson, Consumer Counsel
Frank E. Buckley, Utility Analyst
Mandi Shulund, Secretary

VISITORS PRESENT

Joe Quilici, NorthWestern Corporation
Susan Good, Public Service Commission
Joseph Doyle, Virginia City
Don Quander, Large Customer Group

CALL TO ORDER

The meeting was called to order by Chairman McNutt.

MINUTES OF THE PREVIOUS MEETING

MOTION: Representative Dell moved approval of the minutes of the April 24, 2002 meeting.

VOTE: The motion passed unanimously.

MOTION: Representative Brown moved approval of the minutes of the August 20, 2002 conference call.

VOTE: The motion passed unanimously.

BOB NELSON PROVIDED THE FOLLOWING HIGHLIGHTS OF CASES CURRENTLY PENDING:

NorthWestern Energy, formerly Montana Power Company

D2001.12.156 – MPC Gas Tracker: This gas tracker was filed on 12/7/01 for a $32 million decrease, largely resulting from additional sharing of the proceeds from the gas properties sale. An agreement was reached to spread this decrease out over a few years in order to smooth out rate impacts. MCC also discovered an error that resulted in an additional decrease of approximately $10 million that MPC was authorized to implement on an interim basis. A few issues remained, and George Donkin filed testimony in May on MCC's behalf. Mr. Donkin concluded MPC had incurred costs that were $310,539 too high under an earlier gas buyback contract. Mr. Donkin concluded that MPC terminated that contract three months too soon and therefore incurred increased costs. In addition, MPC also projected to incur costs that were $2.9 million too high. After many discussions, MCC and NWE submitted a stipulation to the PSC on 9/10/02 that agreed to reduce rates by the prior period costs of $310,539 and that gas cost increases resulting from the contract amendment for the projected period would not exceed $970,000. The $970,000 was agreed to based on arguments by NWE that some of those benefits had been realized through the sale to PanCanadian and captured in the sale price that had already been obtained in a prior proceeding. A hearing was held on 9/11/02 and the outcome is still pending.

D2001.10.144 - Default Supply: The PSC issued Final Order 6382d on 6/21/02, finding that final prudence determinations would be made pursuant to the cost recovery mechanism, or when those costs are actually presented, and that there is no requirement for approval of those costs before they are actually incurred. The PSC also concluded that power had been procured from PPL Montana and Duke, which were two large, short and mid-term contracts that complied with industry accepted purchase practices. This was one requirement for recovery

according to HB474. The PSC found that the longer-term resource contracts were proposals and not actual procurements. The Commission clarified that the evaluation of prudence of demand side resources would be conducted in a manner similar to supply side resources and encouraged further analysis of demand side management. A legal conclusion in Final Order 6382d that has bearing on some current issues, including RTO West and the Standard Market Design (SMD), is that default service is a de facto bundled service, which means the PSC has jurisdiction over the transmission component of retail rates. This has been a big issue in the SMD proceeding before the Federal Energy Regulatory Commission (FERC). In this proceeding, FERC has asserted jurisdiction over the transmission component of even bundled rates, but many states are trying to get FERC not to assert jurisdiction over those bundled rates. If those jurisdictional issues are resolved differently than how FERC sees them right now, the conclusion that default service is a de facto, bundled service could have importance in terms of state jurisdiction. The PSC did comment on the proposed resources that NWE had presented in its default supply portfolio, in an attempt to give NWE some assistance in its future direction. The PSC did state that NWE failed to adequately document its judgment and that there had not been a very transparent planning process that the PSC or other parties could refer to in trying to determine prudence of NWE's actions. NWE had not identified and chosen its long-term resources using competitive solicitation, which was a big issue that most intervenors raised. The PSC concluded that the base-load generation projects hadn't complied with industry accepted purchase practices and that NWE had not conducted sufficient due diligence. A statement in Final Order 6382d that is a fundamental conclusion which drives the ultimate result is " The Commission doubts whether NWE would have managed the process similarly if its own money were at risk." This is one of the key issues in the debate about the shifting of risk through pre-approval and trying to maintain the responsibility where the decision-making rests.

With respect to the MFM Plant, the PSC showed concern with lack of fuel information and the potential risks for ratepayers, as well as concern with the

capacity payment issue and the allocation of costs because it was not clear whether or not too much capacity cost was being allocated to the default supply customers. The PSC concluded that the basis for selection of Montana Wind Harness was obscure and selection criteria were not made part of the bid specifications; therefore, other potential bidders didn't have a fair opportunity to participate in the process.

Economic development was discussed at length in this docket and Final Order 6382d stated "The Commission believes that the greatest contribution that it can make to economic development is to focus on setting just and reasonable rates". Commissioners Brainard and Feland stated in a concurring opinion that "Restructuring of the electrical industry means that ratepayers no longer automatically assume the debt incurred by building new infrastructure." Bob felt the premise of that statement was not entirely accurate because he doesn't think that ratepayers automatically assumed that debt in the past. The statement does reflect the concerns about how movement to a competitive generation segment fits with what NWE was trying to propose in terms of pre-approval and having all of these risks allocated away from NWE prior to entering into contracts. Compliance tariffs filed by NWE as a result of Final Order 6382d were based on the QF, Duke, Milltown and PPL contracts as well as some short-term purchases. These tariffs resulted in a 9.96% overall increase for residential customers and the supply component increased 43.9%.

Representative Brown asked if Bob felt that the passage of HB474 helped or hindered the PSC's decision in preparing Final Order6382d. Bob didn't recall any discussion on whether HB474 helped or hindered the decision but said there was an assumption that the decision had to be made pursuant to HB474. Bob also felt that HB474 provided direction for everyone's efforts in the decision making process. Representative Dell said that he felt industry standards that coincide with HB474 were a concern of his in terms of where the legislature went with HB474 but did feel that HB474 was necessary and did help clarify some language. He then asked how Bob thought other states felt with State Public Service Commissions having jurisdiction over transmission rates. Bob stated

that the Supreme Court, in its recent order that affirmed FERC's transmission open access order, did not address whether FERC has jurisdiction over the transmission component of bundled retail rates but did find that FERC has jurisdiction over the transmission component of unbundled rates. NWE's position was that their rates are unbundled, therefore since FERC has jurisdiction over these transmission costs, FERC tariffs would be used instead of State set tariffs. MCC's position was that FERC had not asserted jurisdiction over bundled rates so the PSC had the potential to determine that these rates were bundled and they did retain jurisdiction until there was further development. Other states are concerned about cost impacts and so they appear to be raising all issues possible. Senator McNutt asked Bob how these issues get separated if default service is a de facto bundled service and the MPC customers have unbundled bills. Bob stated that NWE's position is that they have separately stated rates, but MCC feels that there is no real choice for customers and the PSC essentially adopted MCC's position on this issue.

Susan Good from the PSC addressed Representative Brown's question on whether HB474 helped or hindered in making the decisions in Final Order 6382d by stating that in her opinion, HB474 drove the debate on the portfolio question. Ms. Good also responded to Representative Dell's question regarding industry accepted procurement practices being helpful or not helpful. She said that from the PSC's point of view, this was vague in the extreme and there was never a clear definition of what industry accepted procurement practices (IAPP) are. The practices that the PSC ultimately used in determining whether or not IAPP had been applied were the practices that NWE articulated but did not comply with. NWE stated repeatedly throughout their testimony that there were no real IAPP's. Forums are currently being held to discuss procurement guidelines and due to Dr. Wilson's comments on behalf of MCC about pre-approval, NWE has now stated that pre-approval is necessary only to the degree that the procurement guidelines are ambiguous. The PSC does plan on having a draft of the rules ready for review at the 10/8/02 forum. Ms. Good also added that the comments in the SMD Notice of Proposed Rule Making (NOPR)

are due on 11/15/02 and, based on the cost benefit analysis that was done by FERC, Montana did not fare well. Commissioner Anderson has taken a lead among Western States to draw up a proposal and it appears so far to be getting strong support from other Western States.

NWE Advisory Group: NWE has created their own Advisory Group to discuss resource planning and specific concerns about resource acquisitions. Frank attended the first meeting and the discussion to date has focused mainly on renewable resources, although preliminary discussions have begun on their bid processes and contracts that they have been entering into.

D2002.7.80 – Annual Avoided Cost Compliance Filing; QFLT-1 and STPP-1: This filing sets the rates for the QF contracts that have escalation or price adjustment provisions. MCC has reviewed this filing but has not been an active participant because ratepayers will not be affected due to an agreement that fixed the prices related to the QF contracts subject to this filing. Representative Brown asked Bob if NWE could negotiate a better price for those contracts, or is the agreement set so that no matter what happens, NWE will benefit. Bob said that if NWE were to enter into a more favorable agreement than anticipated in the Tier II settlement, which is not likely, NWE would benefit. The prices have been fixed with respect to ratepayers, but both the benefits and risks rest with NWE.

D2002.6.63: Application to Extend Availability of QF-1 (3MW or less) Tariff: This filing is to extend the availability of a QF tariff that relates to 3Mw or less for short-term purchases ending no later than the end of the transmission period. MCC is participating in this case and the rate that NWE is proposing for those QF purchases is the rate that MCC agreed to for the QF projects that NWE previously entered into.

D2002.6.64: BPA Residential Exchange Credit:

This filing relates to Bonneville Power Administration's (BPA) Residential Exchange Credit that results through the financial settlement with BPA and the money flowing back to MPC. This filing is for approval of implementing that credit and a tracking mechanism to handle this credit in the future. MCC did review this filing. Senator Shea asked Bob if this credit was ongoing, and he stated that it is ongoing for a specified period that relates to a settlement of that obligation. Bob will double check on how long this credit would continue and be tracked.

RTO West

RT01-35-005:

MCC filed comments with respect to the RTO West Stage 2 filing within the past few months, focusing mainly on the proposal being incomplete which made evaluating risks and benefits toward customers difficult. MCC commented that FERC should not grant a declaration that the proposal satisfies FERC's requirements. MCC did request that RTO West be required to develop a mechanism to protect Montana at least from negative impacts. FERC did approve the filing and was complimentary of the effort that went into RTO West, indicating that the filing would actually serve as the standard for much of the RTO's that they will be evaluating. FERC also ordered the parties to provide more details, especially with respect to some of the congestion management and governance issues. Senator Shea asked Bob if the actual filing was submitted in May and he said that the Stage 2 filing was submitted in May, but there are filings that preceded that one. Senator Shea also asked how serious MCC comments will be taken by the parties regarding the incomplete details and if they work on providing those details, when can they be expected and will MCC be involved. Bob feels that as the process moves forward MCC's comments will be seriously considered. All of the companies so far have demonstrated an eagerness to work with as many parties as they can because this will be beneficial to them when going back to FERC. The FERC Order will set a timeline for the remaining process.

PP&L

D97.7.91:

This filing relates to Pacificorp and service in North Western Montana. Flathead Electric has filed a motion to intervene in this docket, trying to get the case active again. The restructuring filing for PP&L was filed within days of MPC's restructuring filing, but was processed much more quickly, with the hearing in late 1997. A PSC staff recommendation was issued finding that there were significant stranded benefits that should be flowed back to the customers. The case is currently pending for a PSC decision. In the meantime, Pacificorp sold its distribution system to Flathead Electric so there are potential jurisdiction issues that will need to be addressed by the PSC in order to seek the return of any stranded benefits.

Montana Dakota Utilities

D2002.5.59:

This filing is a gas increase request that relates to non-gas costs, as opposed to a gas cost tracker. MDU had requested an overall increase of 6.5%, or roughly a 20% increase in non-gas costs. MDU proposed to assign all of the increase to small customers, which would mean almost a 9% increase to the residential class, and they also proposed more than doubling service charge rates. The PSC did issue an interim order authorizing an interim increase of 3.7% overall, with an increase of 5.1% to the residential class. Al Clark, Steve Hill and George Donkin filed testimony in mid August on behalf of MCC. Al Clark filed on revenue requirements, Steve Hill on cost of capital and George Donkin on cost allocation and rate design issues. The net affect of the recommendation was that there should be an increase no larger than $2.4 million, which is a 4.23% overall increase. Mr. Clark's recommendation figures to be a little larger than the PSC's interim level, but because of the cost allocation recommendations it would be a little less than what is in the PSC interim order for residential customers. The largest adjustment appeared to be the result of the cost of capital

recommendation, which Mr. Hill recommended at 10.75% return on equity and basically a 50/50 capitol structure, which resulted in a 9.8% overall return. Mr. Donkin concluded that the allocation of those costs in the MDU filing had been too heavily placed on small customers and recommended that there be equal percentage increases. The next step is MDU Rebuttal Testimony and a hearing is scheduled for December.

Monthly Gas Trackers:

MDU files monthly gas cost trackers that MCC reviews on an annual basis. The following four dockets are the monthly gas cost trackers since June:

D2002.6.65

Monthly gas tracker filed 6/1/02, showing a residential net decrease of $.542.

D2002.7.89

Monthly gas tracker filed 7/10/02, showing a residential net decrease of $.339.

D2002.8.101

Monthly gas tracker filed 8/9/02, showing a residential net increase of $.369.

D2002.9.115

Monthly gas tracker filed 9/10/02, showing a residential decrease of $.453.

The current effective rate is $3.649/dk, which does include the 5% increase from the interim order for the non-gas costs.

Mountain Water Company

D2002.5.60:

This filing is for an increase of $1.6 million, which is an overall increase of 13.4%. They have also requested a purchase power tracking adjustment because of the fluctuations that they have been experiencing and the uncertainty surrounding

power costs in the future. They requested a 10.75% return on equity and a 60/40 capital structure. A hearing is scheduled for 11/20/02.

Energy West

D2002.6.77:

This filing is a gas cost tracker proposing a reduction of $9.6 million, or 34.7%, that is reflecting removal of a surcharge and some easing in gas costs. MCC has intervened and is reviewing the case. A hearing is set for 1/15/03.

Energy West will also be filing a general rate case requesting an increase of $1.3 million and have approached MCC about stipulating to a cost of capitol to avoid expenses of processing that part of the case. MCC did enter into a stipulation with Energy West that provides for a 10.61% return on equity and a 50/50 capitol structure. Entering into a stipulation before the actual filing is unusual but beneficial overall because the costs saved by not processing that part of the case will ultimately go back to the ratepayers.

Qwest

D97.2.19, D99.3.68,D2001.1.7, D2000.11.196:

These are applications for approval of interconnection agreements, which are fairly standard. These dockets in particular were filings made as a result of complaints Qwest received from other states saying that Qwest had entered into secret agreements. A secret agreement is where other carriers are not made aware of the pricing terms and therefore would not be able to opt into those pricing terms, which is an option that they have under the Federal Telecommunications Act. Other carriers, primarily AT&T, have used the existence of these types of agreements as an argument against allowing Qwest into interstate service. In response to that, Qwest is looking back to find where secret agreements have been made and are filing them with the state commissions. MCC is reviewing these filings.

D2000.5.70:

This docket pertains to the Investigation into Compliance with §271. This has been on going since 2000 and the issues involved are very complicated. Basically this docket is about trying to verify compliance with the Federal Telecommunications Act of 1996 14-point checklist and other related items. There have been many final reports on various issues by the PSC. The most recent final reports have been on structural separations, public interest and a few other checklist items. MCC did file comments in June on the Operation System Support (OSS), the Change Management Process and a resale billing issue, concluding that Qwest had complied with those requirements.

No. 02-189:

This filing was made by Qwest before the FCC on 7/12/02, requesting approval of In-region InterLATA service. There were actually two filings, one for four states that included Montana and another companion filing that included 9 states. This filing is pursuant to § 271 and required a review of these checklist items as well as certain public interest items, one of those items being the Performance Assurance Plan (PAP). MCC has focused a lot on PAP as a way of insuring against so-called back sliding and making sure that the local markets remain open after Qwest gets interstate approval. As part of this process the FCC is required to consult with State Commissions and the Montana PSC has filed its evaluation of the Qwest application. The PSC recommended approval subject to complying with a few public interest provisions. The first provision was mitigation of what the PSC concluded was a price squeeze in Montana. This was supposedly the result of the difference between carrier access charges that carriers such as AT&T had to pay for gaining access to Qwest customers as opposed to what Qwest was actually charging for its own interstate toll service. The PSC concluded that the price squeeze should be addressed by a significant reduction in access charges, which are a large source of revenue for Qwest. MCC was concerned with this because when access charges are reduced, there is pressure to increase local exchange rates. The second provision the PSC

requested the FCC impose is that Qwest offer reverse line sharing. The reverse line sharing discussion arose because Qwest refused to provide DSL service when competitors gained voice service over a line. MCC filed reply comments to the FCC agreeing with all respects of the PSC's order except the price squeeze issue. MCC argued that there had not been any cost studies performed to show what the costs of access service actually are and that the PSC had been mistaken in attempting to compare the access charge rates to the lowest component of the toll charges. The PSC itself had found earlier that these issues had to be looked at on a service-by-service basis and MCC did not feel that a price squeeze was demonstrated. Qwest must provide these services through a separate subsidiary so there isn't any subsidization happening, which would be a violation of § 271 requirements. MCC's concern here was the pressure that local exchange rates would potentially have due to the price squeeze argument and the reduction of access charges. The PSC did try to accommodate MCC's concerns, and MCC did make similar comments earlier in the PSC's preliminary order. The PSC Final Order said there needs to be an access charge reduction, but they also required that basically a full rate case be filed so that total revenue requirements could be reviewed and any impacts of an access charge reduction could be mitigated by this review. Qwest's recent reports to the PSC indicate that they could be in line for an overall rate reduction, so there was a possibility of some mitigation there. MCC does not want to go into a Montana State jurisdictional rate setting case with an FCC order out saying the premise was reducing access charges when the impact was unknown. MCC did however want to potentially make the case that access charges did not have to be reduced to the extent that the FCC might order. This more or less is a state jurisdictional issue, too, and MCC didn't think it was appropriate for the FCC to get involved. Qwest has withdrawn its application to the FCC because of some accounting problems that they can't verify are in compliance with FCC accounting standards. One requirement of § 271 is that the separate subsidiary providing long distance service has to be in compliance with the FCC accounting standards and because Qwest overall is not in compliance, their subsidiary could

not be found in compliance either. Rather than getting an adverse ruling from the FCC, they withdrew the filing and are attempting to set up an entirely new subsidiary with a new accounting system with the intent to refile and have an expedited proceeding to get FCC approval.

D2002.7.87:

This filing is an application by Qwest to establish cost-based prices for certain Unbundled Network Elements (UNE), which are network elements that competitors access to provide service to their customers as part of the 271 scheme for competition. Some of the prices for the most important UNE's had previously been set but there are many that have not had prices set. This filing had to be made as part of Qwest's compliance with § 271 so the PSC could set those rates, so basically this is a technical issue about appropriate pricing for these UNE's. MCC is reviewing this filing, which is currently in the discovery phase.

CenturyTel

CenturyTel contacted MCC to see if accommodation on an alternative regulation plan could be reached, prior to the actual filing. They provided an outline of their thoughts on alternative regulation and MCC indicated interest to discuss this. In the past, MCC has favored alternative regulation plans given certain conditions and did provide some very brief comments, basically asking for more information. CenturyTel subsequently indicated that they have suspended work on this and that they didn't intend to pursue an alternative regulation plan filing. Senator Shea asked Bob why he thought they chose to do this. Bob wasn't sure why, but he speculated they may want to avoid a review of additional items.

Default Supply Inquiry

There are ongoing default supply activities at the PSC and in contrast to the Advisory Committee for NWE these are activities that are being conducted under the direction of the PSC.

D2002.7.93:

This filing is a formally docketed inquiry into default supply that is basically attempting to determine what the necessary and reasonable roles for default supply service are. The PSC requested comments on 14 questions that they had issued and MCC filed comments on 8/26 that were generally supportive of the PSC default supply final order. The bottom line of MCC's comments were that the default supplier should seek to provide the lowest cost and most efficient service possible given the load characteristics of its customers. Ms. Good commented that there are still meetings going on in this docket to discuss those comments and they have been very effective. The first three meetings included participation only from parties that supplied written comments. Now that input has been gathered, the meetings now are more toward putting guidelines together. After the 10/22/02 meeting, there will be draft guidelines given to the PSC that they can use however they would like, for example, for adopting guidelines or as a draft order. The toughest phase of the meetings will then be establishing rules for choice and moving to competition. These issues have already proven to be extremely contentious and it is beneficial that the procurement guidelines will be set up first.

Energy Forum

The Energy Forum was originally intended to address a few issues, such as rate design and default supply. The focus so far has been exclusively on default supply. Overall an attempt has been made to mitigate default supplier risks by defining default supplier obligations. Senator Shea asked if the discussions would ever be held outside of Helena and who is notified of these meetings. Ms. Good stated that so far the meetings have been held at the PSC and that there is a large service list used to notify people of the meetings and there have also been notices published in the Great Falls Tribune. To her knowledge, this has been the first time that all different stakeholders have sat down to discuss default supply issues. With the help of these forums, the PSC is committed to gathering feedback and allowing all stakeholders to speak their minds through the 14

questions. Senator Shea asked if there would be a summary of these discussions and if so, how copies can be obtained. Ms. Good mentioned that the questions and all responses are available on the PSC Website. Joe Quilici addressed Senator Shea's questions by adding that NWE sent out a document called "Comments Regarding Electric Supply Service" regarding the 14 questions that the PSC requested comments to and he will make sure that all Committee members get a copy of this document.

FERC

RM01-12-000: Remedying Undue Discrimination Through Open Access Transmission and Standard Electricity Market Design.

The cornerstone of this docket is Remedying Undue Discrimination, which is the requirement under the Supreme Court order for FERC's assertion of jurisdiction over all transmission rates, including bundled retail transmission. Several Montana parties met at the request of NWPPC to discuss issues with respect to the SMD NOPR. A list of issues was developed at that meeting and assignments were made to various parties to create initial memos that are due later this month. The intent is to file joint comments because there will be similar views on some issues. Comments due are due 11/15/02 with replies being due 12/20/02. The purpose of this NOPR was to insure adequate generation resources and establish a platform for exchange of electricity and transmission. This particular FERC NOPR is different from prior transmission NOPRs because they are trying to get at both generation and transmission and insure that there is a liquid market for generation and no congestion that precludes generation resources from being sold from one region to another. Some history on this is the first order issued, Order 888 in 1996, required open access transmission, which flowed out of the Federal Power Act of 1992. FERC was trying to require open access transmission so that a utility would provide services to anyone who wanted to get on their transmission system. A few years later, Order 2000 was issued because they found there were still discriminatory practices where utilities were discriminating in favor of their own load. A footnote to this is that there was a

presentation to the Transition Advisory Sub-Committee on 9/13/02. Marilyn Showalter, Chair of the Washington State Commission, stated that the premise of the FERC NOPR is to eliminate undue discrimination and in her view, especially in a state like Washington where they are still fully integrated and regulated, there should be discrimination in favor of the native load of regulated utilities customers. Bob stated that they have a very fundamental problem with this that may not be the same problem Montana has with a restructured environment and no generation owned as part of a vertically integrated utility. In Order 2000, FERC encouraged transmission-owning utilities to turn operational control over to independent RTO's, which spawned all of the RTO West filings and RTO's in other regions. FERC has concluded that there is still undue discrimination in that arrangement so they have proposed the SMD NOPR. This NOPR is needed because of the absence of standardization within and between regional markets that creates some discrimination and inefficiencies between these RTO's that tend to raise costs. These utilities still tend to favor their own generation by interrupting competitors generation to solve reliability problems rather than their own. As a result of this, FERC found that rates are unjust and unreasonable and are going to establish a two-tier oversight for regional transmission organizations or what they are calling Independent Transmission Providers (ITP). There will be a governing board of independent directors, which means they cannot have a market stake in anything that is going on. The second tier is an advisory committee of State Officials and market participants. Losing state jurisdiction was also a point that Marilyn Showalter voiced concern over. Her statement was that an advisory role is not an authority role, so any advice given by them does not have to be taken. This could be a significant concern to many people who are opposing this SMD proposal. Some specifics of the proposal are that there will be ITP's that will administer spot markets and FERC envisions that most transactions will occur in bilateral markets, not in spot markets. Spot markets will be developed for wholesale power, ancillary services, transmission congestion rights, real time balancing and day ahead market. These spot markets are critical to determining some of the other elements, such as locational marginal

pricing and congestion revenue rights. The locational marginal prices are determined and based on market clearing prices at various nodes and the difference between those market clearing prices. Those prices will basically be driving the transmission costs. With concerns about existing customers losing their current contract rights, FERC has included provision to secure transmission through congestion revenue rights. The existing transmission owners and users will get rights to use that transmission. For existing utility users like NWE there will be a four-year window where they will be automatically assigned those congestion revenue rights. When people try to buy their way through congested pieces of the transmission system, they will be paying locational marginal prices and the holder of the congestion revenue rights gets the revenues for the congestion. The theory is that the existing utility users will not be harmed since they are getting the revenues back that they bid. All of the transmission tariffs are going to be network tariffs and right now, there is a combination of network tariffs and point-to-point tariffs. The network concept is that power providers can pay on any point on the transmission system and take power out on any point. There are also point-to-point tariffs, where the rights to transmit power from one point to another can be purchased. Under this SMD proposal there will be no point to point service, there will only be network tariffs due to concern that there was discrimination with respect to point to point transmission tariffs. There is a requirement for generation adequacy that load serving entities, including NWE and MDU, maintain a 12% reserve margin in resource supply. There is a lot of discussion in the SMD about demand response being on equal footing with the supply side and there is a requirement that demand response also be able to be bid into these spot markets. A major component of this proposal is that there would be active market monitoring and mitigation, so each RTO will have to have market monitors to make sure that there is no gaming of the system and the ability to mitigate any market problems on an expedited basis. FERC has indicated the timeframe of two years for implementation. Some states are concerned about participant funding and through-and-out pricing, both related to recovery of the transmission investment. Governors in some southern states

have made complaints about this and not wanting to take the responsibility of transmission costs incurred to provide service out of their jurisdiction. FERC has essentially agreed with them on this and they were successful in putting a requirement into a FERC funding bill that states before FERC can implement these rules, a cost benefit study must be done on which regions are going to suffer and which regions will benefit through the allocation of these kinds of costs. The through-and-out issue relates to if an energy purchase is made through RTO West, but does not serve load in RTO West, then RTO West does not receive any money for that, even though the purchaser is using the transmission facilities of RTO West, which creates a significant cost shifting concern. Currently those transactions are allocated costs and revenues come back and offset other rates. Those revenues would disappear. There is a concern for many states about increased energy prices and it has been indicated that there is going to be upward pressure on prices in Montana because the export of power makes it easier to get out of state. Regional differences are also a concern. One regional difference is the need for various levels of reserve margins and another is that FERC is requiring market bid caps that the market monitor will be able to impose if things get out of control. Some commenters believe that the standardized market bid cap is probably not a good idea because every region has its own situation. For example, MCC might contend that utilities in Montana exercise more market power than a utility in New Jersey, so Montana market bid caps may need to be different than New Jersey's. There is also a concern on governance, or how a meaningful role for state regulators for oversight of these RTO's is worked out.

Wettington Water System

D99.5.136:

Wettington Water Systems have made a request for a flat rate increase from $25 to $60. Also requested are disconnect and reconnect fees of $25, non-payment reconnect fee of $75 and delinquency fees of $25 with $2 a day over 20 days. MCC has intervened and will be reviewing their proposal.

Five Valleys Gas

D2001.5.59:

This filing proposes transfer of ownership of propane service in the Seeley Lake area to Energy Partners. After reviewing the proposal, MCC had no objections to the transfer but wanted to leave this open since they had not actually provided the contract they were describing. MCC did not object when the contract was provided and the PSC issued a final order approving the transfer of ownership.

Firelight Meadows

D2001.12.174 and D2001.12.175:

Firelight Meadows is a new utility for water and sewer service that filed a request for initial rates. Since this was a filing for initial rates, there was no historical data available to judge the reasonableness of their filing. MCC recommended to the PSC that they allow an interim period of two years to collect actual data. The PSC did issue interim orders in late May.

Havre Pipeline

D2002.8.99:

A gas tracker was filed for a rate decrease of 37.5%. MCC has intervened and will be reviewing this filing. Havre pipeline is on an annual tracker.

PUBLIC COMMENTS

Mr. Joseph Doyle from Virginia City stated his concern about Virginia City water and sewer rate increases not being appropriately filed with MCC. He stated that for three years he has been dealing with MCC on this issue and has also spoken to Senators McNutt and Shea. Mr. Doyle feels that it has come to the point where he needs to speak up about not having gotten a simple answer to a simple question. Bob offered some history by stating that municipal water and sewer utilities were largely deregulated in the early 1980's because they had a 12%

band in which they could increase rates within their own authority, or if the cause of the rate increase was a mandated improvement by the Federal or State authorities, then those costs could be flowed through without PSC approval. After those exceptions were incorporated into laws, there were very few municipal rate applications that came to the PSC. The filings that did come through to the PSC, resulting from complaints or utility filings, were somewhat problematic for the PSC in trying to determine whether they met these exception requirements. In the early 1990's a proposal was made to entirely deregulate municipal water utilities and remove them from PSC jurisdiction, which the PSC supported because they found the then current arrangement unworkable. This legislation passed and the municipal authorities were given full discretion to run their utilities. When the PSC was removed, the provision relating to MCC's office was not so MCC is still involved in receiving complaints from customers and can technically take the municipal government to court if it is felt that they have violated rate making requirements. Unlike the PSC, the municipalities have very few rate making requirements that are imposed by law, so MCC has very little in the way of rate making standards to actually review, especially with the municipalities given broad discretion to set rates and requirements for service. In spite of these difficulties, over the years MCC has tried to entertain complaints and work out arrangements between customers and municipalities, and have had some successes, mainly related to clear-cut violations of requirements that municipalities have engaged in. Another area that MCC has been particularly interested in is notice requirements for the customers of those utilities. MCC has had some success in the past in concluding that customers had not been properly noticed of rate increases.

After reviewing the Virginia City file, Bob's understanding was that this case started with a complaint that a particular service charge was being assessed, even though water was turned off, and there was an issue whether that rate, that the city adopted an ordinance on, had been adequately noticed. MCC's inquiry in that case was whether Virginia City provided notice to the customer that filed the complaint, or to the customers in general, about this rate

increase, and whether customers had the opportunity to participate. Bob felt that MCC was stonewalled in the request to get that information from Virginia City. There is a series of letters that relate to Tom Muri's communication with Virginia City, but information was never completely forthcoming, causing communication lapses between requests. In May 2002, just before Tom left, MCC received a copy of notices and more details about these water and sewer issues. Tom confirmed to Bob that he believed this information resolved the issue with respect to notice to the customers. But apparently this information did not resolve all of the issues. Mr. Doyle said that he has been trying for a long time to resolve this issue of notice to MCC, but this spring was the first time that Bob was aware that notice to MCC was an issue. Having confirmed the notice to the customers, Bob's conclusion was that Virginia City neglected to notice MCC. There is a provision in law, because of MCC's continued involvement, that they were to serve MCC with notices of increases so that MCC can participate if needed. Bob's reaction to this is that if the issue now was MCC's right to a hearing and the violation of notice to MCC, then MCC could possibly pursue this issue with Virginia City to try to get a hearing opened. Before this was done, Bob wanted to satisfy in his mind that there was an ultimate issue beyond the notice issue that MCC wanted to pursue. In other words, once a hearing was opened, what is it that needs to be resolved? In the most recent letter to Mr. Doyle, Bob asked for specific information on substantive issues so MCC can evaluate the information and make a decision about pursuing the apparent notice violation. Bob's view is that it would be more productive to go into discussions fully knowing what it is MCC ultimately wants to pursue. Mr. Quilici stated that he was involved in this procedure years ago and remembers when the municipalities came before the legislature asking for this section of the statute to be amended. One reason they gave was since the local governing body is elected by the ratepayers of these water districts, the elected officials represented the people themselves. Most municipalities are not following the amendment to notice MCC and there was a time when municipalities wanted to raise a water rate more than 12%, they had to go before the PSC, therefore before MCC. Senator Shea reiterated that there

have been communication lapses in the small conversations between herself, Senator McNutt and Mr. Doyle. Senator Shea asked Bob if he was aware of any notification from Virginia City. Bob stated that the initial complaint that is in MCC's file, was actually from another individual other that Mr. Doyle. Mr. Doyle stated that person was Connie Loeberg and said that complaint was that the expansion of the water system should have been, a fire district issue instead of a rate increase passed on to the consumers of Virginia City and had MCC stepped in at that point it would have alleviated all the questions on the next two sewer issues that have taken place over the last two or three years. Mr. Doyle does not have all that information because the people that he has tried to get information from, including the City Clerk, Treasurer, and the Mayor's Office have stonewalled him as well, and that is where he has asked MCC to step in. Mr. Doyle did recognize that MCC has capable people on staff and he would like someone to step in to look at this information. Bob, commenting on Mr. Doyle's statement about the fire district issue, stated that the original complaint that MCC got was specifically about the assessment of service charges, when service was not turned on. According to MCC's written records, there was no mention of the fire district or anything similar to that. Bob's belief and recommendation is that for this case to move forward, there should be a specific and clear listing of the issues that Mr. Doyle or anyone who is bringing the complaint forward believes that MCC should pursue. This way MCC can be aware of the issues and can take those to a review with Virginia City, rather than just going to them with a general and vague understanding of what the issues may be and if they are even issues that MCC should be pursuing. Senator Shea verified that Mr. Doyle should put together, with whomever he needed to, a list of complaints and/or issues that he feels need to be addressed and then formally submit them to Bob. Bob stated that this is his prefereance and feels that this is the clearest way to communicate. Bob understands Mr. Doyle's frustrations since this has been going on so long. However, this is what needs to be done to move forward. Mr. Doyle has no problem doing this if he could get the necessary info from Virginia City and he asked that MCC ask Virginia City to provide the supporting

documents for everyone to review. Mr. Doyle has tried to get records such as tapes of public hearings, but understands that those have been destroyed and is unsure how this fits into statute. He feels that he has been constantly stonewalled when asking for information, and stated that it is difficult for him to produce information that MCC wants without getting substantive information from Virginia City. Senator McNutt asked if Mr. Doyle would send to Bob a list of complaints and issues as a constituent of the water district without all the behind the scenes information such as public hearing tapes. Mr. Doyle said that he could do that, but he feels that things should be done the other way around and that Virginia City should provide MCC with the information. Senator Shea stated that MCC does not know what to ask for if the issues and complaints are unknown to them. Mr. Doyle feels that what MCC should ask for is what Virginia City should have provided in the first place. Mr. Doyle offered information to MCC some time ago and understands that MCC's file may not be as complete as his. Mr. Doyle stated that at one time they had an attorney involved and he would be glad to talk to that attorney about coming to Helena to go through the two files with MCC. Bob wanted the committee to be aware of how MCC typically handles these issues. Municipalities are actually only required to file a notice of increase, no justification or any other information. Bob mentioned that he wouldn't be surprised if a majority of the municipal governments are in violation of that notice provision in adopting their rates. MCC's approach has been to react to specific consumer complaints and because of resource constraints, MCC typically only gets involved when there is a complaint with some specifics presented, this way MCC can request more detailed information. MCC is in a reactive mode, which is different than how MCC operates with other utilities because of the status of municipal water and sewer. Bob stated that some people may think a notice or reminder should go out reminding the cities that they need to notify MCC and that way all cases could be review independently. This process would create a significant workload issue for MCC and Bob is not convinced that it would be very productive due to discretion the cities have been given to regulate their own rates. MCC does get involved if a particular complaint comes in that it appears

MCC can be helpful in. Senator McNutt reiterated the request that Mr. Doyle follow up on this. Mr. Doyle thanked the Committee for their time.

FINANCIAL REPORT

The financial summary for August, 2002 was presented. Bob stated that it was only for the first two months of the fiscal year and didn't indicate any significant issues or concerns. With MCC being 40% understaffed, salaries are well behind where they would normally be.

BUDGET

FY04 and FY05 budget proposals were primarily based on actual FY02 levels, as well as Department of Administration fixed costs and inflation/deflation, with a few exceptions. Personal services reflected currently approved levels, set within the FY03 budget, with no amounts included for base salary or benefit increases. Contracted services can fluctuate radically from year to year and FY02 turned out to be higher than usual. For FY04 and FY05 proposals, contracted services was adjusted by averaging FY01 and FY02 and then inflating to FY04 and FY05 values with 2% and 1% inflation factors. In addition, the contingency amount was reduced from $200,000 to $125,000. The approach here was to bring the contingency to the purchasing power it had 10 years ago. A minor increase in communications was added for the possible need to advertise job openings. FY02 was a historical low for travel, due to workload and staff availability for travel, so it wasn't prudent to budget based on that figure, especially with what the workload appears to be in the future. FY04 and FY05 travel proposals are based on a review of the past 4-5 years and the FY04 proposal would be the lowest request in the past 10 years, being about 30% lower than FY99.

Bob feels that these proposals are conservative yet realistic. Fy04 is 2% smaller than the FY03 budget, and FY05 will also be somewhat less. Bob also feels that overall the budget is reasonable in view of the benefits that MCC

returns to the consumers. With committee approval, the next step would be the regular legislative process.

MOTION: Representative Brown moved approval of MCC's budget as presented to the committee.

VOTE: The motion passed unanimously.

Adjournment

There being no further business to come before the committee, the meeting adjourned.

Respectfully submitted,

_____, Robert Nelson, Consumer Counsel

Accepted by the Committee this _____ day of _____, 2002

_____, Chairman